

June 24, 2004



Logistics

Navy Controls Over Materiel Sent to Defense Reutilization and Marketing Offices

(D-2004-095)

Department of Defense
Office of the Inspector General

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Report Documentation Page				Form Approved OMB No. 0704-0188	
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1. REPORT DATE 24 JUN 2004		2. REPORT TYPE N/A		3. DATES COVERED -	
4. TITLE AND SUBTITLE Logistics: Navy Controls Over Material Sent to Defense Reutilization and Marketing Offices				5a. CONTRACT NUMBER	
				5b. GRANT NUMBER	
				5c. PROGRAM ELEMENT NUMBER	
6. AUTHOR(S)				5d. PROJECT NUMBER	
				5e. TASK NUMBER	
				5f. WORK UNIT NUMBER	
7. PERFORMING ORGANIZATION NAME(S) AND ADDRESS(ES) Department of Defense Office of the Inspector General 400 Army Navy Drive Arlington, VA 22202				8. PERFORMING ORGANIZATION REPORT NUMBER	
9. SPONSORING/MONITORING AGENCY NAME(S) AND ADDRESS(ES)				10. SPONSOR/MONITOR'S ACRONYM(S)	
				11. SPONSOR/MONITOR'S REPORT NUMBER(S)	
12. DISTRIBUTION/AVAILABILITY STATEMENT Approved for public release, distribution unlimited					
13. SUPPLEMENTARY NOTES					
14. ABSTRACT					
15. SUBJECT TERMS					
16. SECURITY CLASSIFICATION OF:			17. LIMITATION OF ABSTRACT UU	18. NUMBER OF PAGES 31	19a. NAME OF RESPONSIBLE PERSON
a. REPORT unclassified	b. ABSTRACT unclassified	c. THIS PAGE unclassified			

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Acronyms

DAAS	Defense Automatic Addressing System
DLA	Defense Logistics Agency
DEMIL	Demilitarization
DRMO	Defense Reutilization and Marketing Office
DRMS	Defense Reutilization and Marketing Service
DTID	Disposal Turn In Document
ICS	In-transit Control System
NADEP	Naval Aviation Depot
NAVICP	Naval Inventory Control Point
RRAM	Realtime Reutilization Asset Management



INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
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June 24, 2004

MEMORANDUM FOR NAVAL INSPECTOR GENERAL
DIRECTOR, DEFENSE LOGISTICS AGENCY

SUBJECT: Report on Navy Controls Over Materiel Sent to Defense Reutilization and
Marketing Offices (Report No. D-2004-095)

We are providing this report for information and use. We considered management comments on a draft of this report when preparing the final report.

Comments on the draft of this report conformed to the requirements of DoD Directive 7650.3 and left no unresolved issues. Therefore, no additional comments are required.

We appreciate the courtesies extended to the staff. Questions should be directed to Terry Wing at (215) 737-3883 (DSN 444-3883). See Appendix B for the report distribution. The team members are listed on the inside back cover.

By direction of the Deputy Inspector General for Auditing:

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Office of the Inspector General of the Department of Defense

Report No. D-2004-095

(Project No. D2003LD-0081)

June 24, 2004

Navy Controls Over Materiel Sent to Defense Reutilization and Marketing Offices

Executive Summary

Who Should Read This Report and Why? Logistics personnel responsible for disposing materiel that is excess to DoD requirements should read this report since it addresses needed in-transit control improvements.

Background. The Defense Reutilization and Marketing Service (DRMS) is an organization within the Defense Logistics Agency that is responsible for the reutilization, transfer, donation, sale, and disposal of materiel that is excess to DoD requirements. In FY 2002, Defense Reutilization and Marketing Offices, which are field offices of DRMS, received approximately \$15.8 billion (acquisition cost) worth of materiel for disposal. Of the \$15.8 billion, \$2.1 billion of materiel was received from Navy organizations. Navy organizations that ship materiel to DRMS are required to provide shipment notification transactions to DRMS. DRMS maintains an in-transit control system based on shipment notification transactions in order to monitor shipments of usable materiel with a line-item value of \$800 or more and for all shipments of pilferable or sensitive materiel, regardless of dollar value.

Results. The controls over materiel designated for or sent to DRMS need improvement. Some materiel that was reported as shipped to disposal was neither recorded as received at DRMS nor accounted for on inventory records, and Navy organizations did not send proper disposal shipment notifications to DRMS. Defense Logistics Agency storage depots did not properly account for materiel awaiting demilitarization instructions and DRMS management data was inaccurate and not properly utilized. A judgmental sample of 700 Navy disposal transactions, valued at \$134.3 million, indicated that only 349 transactions, valued at \$34.1 million, were properly recorded as received by DRMS. Of the remaining 351 transactions:

- 147 transactions, valued at \$37.7 million, were not recorded as received by DRMS and were not recorded on accountable supply records (\$32.3 million of the \$37.7 million worth of materiel was located with the assistance of depot personnel);
- 5 transactions, valued at \$4.1 million, were recorded as partial receipts by DRMS, with some materiel recorded as received (\$2.8 million) and some materiel neither recorded as received nor accounted for on accountable supply records (\$1.3 million); and
- 199 transactions, valued at \$58.4 million, were erroneously reported to DRMS as disposal transactions.

As a result, \$39 million worth of Government property that was not recorded on accountable supply records was vulnerable to loss or undetected theft, and resources could be expended unnecessarily in researching erroneous disposal transactions. The Commander, Naval Supply Systems Command, should establish controls to ensure that Navy organizations comply with procedures to account for materiel designated for shipment to disposal. The Director, Defense Logistics Agency, should establish controls over materiel requiring demilitarization and require DRMS to review and analyze management data. (See the Finding section of this report for the detailed recommendations.) We reviewed the management control program as it related to controls over repairable and consumable assets that the Navy determined to be excess or uneconomical to repair. Management controls over assets did not ensure that materiel was shipped to or received by DRMS.

Management Comments. The Navy and the Defense Logistics Agency concurred with the recommendations and the Navy also agreed to identify shipments to disposal as an assessable unit as part of its 2004 management control program. See the Finding section of the report for a discussion of management comments and the Management Comments section of the report for the complete text of the comments.

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Background

Defense Reutilization and Marketing Service. The Defense Reutilization and Marketing Service (DRMS) is an organization within the Defense Logistics Agency (DLA) that is responsible for the reutilization, transfer, donation, sale, and disposal of materiel that is excess to DoD requirements. In FY 2002, Defense Reutilization and Marketing Offices (DRMOs), which are field offices of DRMS, received approximately \$15.8 billion (acquisition cost) worth of materiel for disposal. Of the \$15.8 billion, \$2.1 billion of materiel was received from Navy organizations.

DoD Guidance. DoD Manual 4000.25-1-M, “Military Standard Requisitioning and Issue Procedures,” February 11, 2002, provides procedures for processing shipments of materiel to DRMOs. DoD organizations are required to prepare a disposal turn-in document (DTID) that accompanies disposal shipments and to provide a shipment notification transaction to DRMS for each shipment of materiel to DRMO. If a shipment notification transaction is for either usable property with a line-item value of \$800 or more or for a shipment of pilferable or sensitive materiel regardless of dollar value, DRMS establishes a due-in for the shipment in the in-transit control system (ICS). The ICS provides for the in-transit control of materiel shipped to DRMO from the time a due-in is established until the receipt of the materiel by DRMO.

When materiel is received at DRMO, DRMO processes a receipt transaction. If the transaction meets the criteria for inclusion in the ICS, the transaction is compared with dues-in previously established in the ICS. If the receipt transaction matches a due-in, the due-in will be closed. If, after 90 days from the date DRMO posts a receipt transaction there is no matching ICS due-in, DRMS sends a disposal receipt confirmation follow-up transaction (document identifier code AFX with advice code 36) to the organization identified in the receipt transaction. That follow-up transaction alerts the organization that materiel was received without the required shipping notification transaction. DoD organizations are not required to respond to that follow-up transaction.

DRMS sends a disposal shipment confirmation follow-up transaction (document identifier code AFX with advice code 37) if, after 90 days, there is no receipt for an ICS due-in. DoD organizations are required to respond to that follow-up transaction by reviewing shipping documentation and providing the status to DRMS. If either the materiel or status is not received by DRMS within 30 days of that follow-up transaction, a second disposal shipment confirmation follow-up transaction (document identifier AFZ with advice code 37) is sent. A due-in remains open for 1 year from the date established if either the materiel is not received or the status is not provided. After 1 year, the due-in is transferred to a history file.

Prior and Related Audits. The Inspector General of the Department of Defense and the General Accounting Office have previously issued reports that addressed weaknesses in controls over materiel shipped to DRMOs (Appendix A). In response to recommendations in those reports, DoD convened an Integrated Process Team to examine and resolve problems with materiel in-transit to DRMOs. As a result of the team’s evaluation, a training web site was created with an instruction guide that stresses accountability and responsibility for disposal shipments. Additionally,

DoD Manual 4000.25-1-M was revised to require edits of shipment notification transactions to prevent erroneous transactions from passing between shipping organizations and the DRMS, and the ICS was changed to revise the criteria for matching in-transit transactions and the time frames for sending DRMS follow-up transactions.

Objectives

The initial overall audit objective was to evaluate the process used by the Navy to dispose of repairable assets, and we planned to specifically evaluate the controls in place to ensure that repairable assets managed by the Naval Inventory Control Point (NAVICP) and identified as excess or uneconomical to repair were appropriately disposed of and received by the DRMS. However, based upon our survey work, we revised the objective to evaluate the controls in place for both consumable and repairable assets that the Navy identified as excess or uneconomical to repair, regardless of the inventory manager, to determine if the assets were received by the DRMS. We also reviewed the management control program as it related to the revised audit objective. See Appendix A for a discussion of the scope and methodology, our review of the management control program, and prior coverage related to the objective.

Management of the Disposal Process

The controls over materiel designated for or sent to DRMS by the Navy needed improvement. Specifically, accurate accountability over property in-transit was lacking. Based on a judgmental sample of 700 Navy disposal transactions, valued at \$134.3 million, for the period of March 2002 to July 2003:

- 349 transactions, valued at \$34.1 million, were properly recorded as received by the DRMS;
- 147 transactions, valued at \$37.7 million, were neither recorded as received by the DRMS nor recorded on accountable supply records (\$32.3 million of the \$37.7 million worth of materiel was located with the assistance of depot personnel);
- 5 transactions, valued at \$4.1 million, were recorded as partial receipts, with some materiel recorded as received (\$2.8 million) and some material neither recorded as received nor accounted for on accountable supply records (\$1.3 million); and
- 199 transactions, valued at \$58.4 million, were erroneously reported to the DRMS as disposal transactions.

Those conditions occurred because of non-compliance with existing guidance, computer programming errors, and lack of management oversight. As a result, \$39 million worth of Government property not recorded on accountable supply records was vulnerable to loss, and resources could be expended unnecessarily in order to research erroneous disposal transactions.

Criteria

Navy Procedures. Naval Supply Systems Command (NAVSUP) P-485, "Ashore Supply," June 1998, provides procedures for the control of in-transit materiel shipped to DRMOs. Navy organizations are required to provide a disposal shipping notification to DRMS at the time materiel is physically shipped or transferred to a DRMO. Organizations that do not have the capability of preparing disposal shipment notifications should work through a support activity to ensure that shipment documentation is correct and is sent to DRMS. Supply organizations that receive DRMS follow-up transactions are required to review the transactions to ensure that appropriate research is conducted. Supply organizations are also required to ensure that shipping organizations review receipt documentation, investigate discrepancies, and provide timely responses to DRMS follow-up transactions. Responses to DRMS follow-up transactions should reflect the results of research rather than an automatic computer generated response. Quantities of material that are dropped from accountable records should be matched against the quantities that have actually shipped. Diligence in researching DRMS follow-up transactions is essential to the integrity of the ICS system. When evidence exists that unresolved discrepancies are

the result of theft or other forms of fraudulent activity, organizations are required to report the discrepancies to the appropriate criminal investigative office.

DoD Manual. DoD Manual 4160.21-M-1, “Defense Demilitarization Manual,” February 1995, provides guidance for the demilitarization of materiel by the Services. The manual states that the Services shall establish and maintain Special Defense Property Disposal Accounts and will maintain responsibility for ammunition, explosives and dangerous articles, classified material, inert material, small arms weapons, and any items that require demilitarization (demil), declassification, or reclamation prior to the physical and accountable transfer of materiel to DRMO. DoD item managers are to assign a demil code to identify materiel that must be demilitarized. The instruction further provides that, depending on the assigned demil code, some disposal transactions require demilitarization or disposition instructions before the materiel can be shipped to and accepted by the DRMO.

DLA Instructions. DRMS Instruction 4160.14 Vol. IV, “Policy and Procedures In Disposal Operation for Property Accounting and the Defense Reutilization and Marketing Offices,” November 2003, defines demil as the act of destroying the militarily offensive or defensive advantages inherent in certain types of materiel.

Defense Distribution Depot Memorandum, “Instructions for Holding Disposal Release Orders for Materiel with Demilitarization Codes ‘F’, ‘G’, or ‘P’,” June 2003, requires that DLA storage depots do not ship materiel with demil codes F, G, or P to disposal facilities until disposition instructions are obtained from the DoD item manager. The memorandum states that DLA distribution depots are responsible for maintaining control and accountability of all Navy materiel until it is shipped from the depot. If the depot does not receive disposition instructions within 21 days of the receipt of a disposal transaction, the depot is to reverse the disposal transaction and add the materiel back to the inventory records. If the materiel is not added back to the inventory records, there is no accountability and visibility of the materiel.

Materiel Designated for or Shipped to Disposal

The controls over materiel designated for or sent to DRMS by the Navy needed improvement. Some material was erroneously reported to DRMS as having been shipped to disposal, and materiel identified as having been shipped to disposal was sometimes neither recorded as received at the DRMS nor accounted for on supply records. Those conditions occurred because of non-compliance with existing DoD and Navy guidance for processing materiel to disposal.

To determine if materiel designated for or sent to disposal was received at DRMOs or otherwise accounted for, we selected judgmental samples of 700 disposal transactions, valued at about \$134.3 million, that were processed by 13 Navy organizations and 2 contractors that repair Navy repairable assets. The 700 disposal transactions were selected from either a database provided by the Defense Automatic Addressing System (DAAS) of follow-up transactions for materiel reported as shipped but not received, a database of disposal shipments provided by NAVICP, or disposal shipments selected from the supply records of the 15 organizations evaluated. See Appendix A for discussion of the sampling selection methodology.

Of the 700 disposal transactions reviewed, 349 transactions, valued at \$34.1 million, were properly recorded as received by DRMS. The remaining 351 transactions, valued at \$100.2 million, were either not recorded or partially recorded as received at the DRMS or represented an erroneous disposal transaction.

Disposal Transactions. Of the 351 transactions, 147 transactions, valued at \$37.7 million, were neither recorded as received at DRMS nor recorded on accountable inventory records, and 5 transactions, valued at \$4.1 million, were recorded as only partial receipts, valued at \$2.8 million. The remaining \$1.3 million of the \$4.1 million was neither recorded as received at DRMS nor recorded on accountable inventory records. Of the \$39 million (\$37.7 million plus \$1.3 million) worth of materiel that was neither recorded as received at DRMS nor recorded on accountable supply records, materiel related to 34 transaction, valued at \$32.3 million, was located, during our review, with the assistance of depot personnel. Of the 147 transactions:

- 33 transactions were for materiel that required demil and was not shipped to DRMS,
- 27 transactions were for materiel that was not shipped to DRMS but which was located in the warehouse,
- 87 transactions were for materiel that was recorded as shipped to DRMS but was not located.

Demil Items. For 33 transactions valued at \$35.7 million, materiel was dropped from accountable supply records but not shipped to DRMS because the Navy either did not provide demil instructions to DLA depots or when the demil instructions were provided, DLA depots did not act on them. Additionally, DLA depots did not follow-up with Navy organizations when instructions were requested and not received and did not take action to add the materiel back on to inventory records to provide accountability and visibility of the materiel. The 33 transactions consisted of items that had been assigned a demil code of either F or P. Demil code F materiel requires demilitarization instructions to be furnished by the item manager before processing the disposal transaction to the depot. Demil code P materiel must be demiled before processing the disposal transaction to the depot. With the assistance of DLA depot personnel, we were able to locate materiel related to seven transactions, which was valued at \$32.2 million.

Of the 33 transactions, materiel related to 25 transactions, valued at \$3.5 million, was considered sensitive or pilferable. For example, on August 5, 2002, a pilferable valve, valued at \$5,906, was dropped from the accountable inventory records without the required disposition instructions having been provided by the Navy. As of September 25, 2003, the depot had not requested the demil instructions and had not taken action to reverse the disposal transaction. As a result, there was no accountability or visibility of the materiel for almost 14 months. Additionally, none of the \$3.5 million worth of materiel could be located.

Materiel Not Shipped. For 27 transactions valued at \$65,000, the materiel had been dropped from the Navy accountable records; however, the materiel had not been sent to DRMO by the shipping organization. The shipping organization, Naval Air Station Patuxent River, Maryland, advised us that it had located the materiel and, as a result of our audit, would review materiel in its storage facility to ensure that materiel designated for disposal was shipped to disposal.

Materiel Not Located. Materiel related to 87 transactions, valued at approximately \$1.9 million, was not recorded on accountable supply records and could not be located. Of the 87 transactions, materiel related to 35 transactions, valued at \$1.1 million, was considered pilferable. For example, at the Defense Depot San Diego, California, a pilferable enclosure assembly, valued at \$37,680, was not recorded as received by DRMS and could not be located at the depot as of October 31, 2003. The enclosure assembly was dropped from Navy inventory records on October 22, 2002.

Materiel Partially Received. For five transactions, valued at \$4.1 million, \$2.8 million worth of material was recorded as received by DRMS, and \$1.3 million worth of material was not recorded as received and could not be located by the shipping organizations.

Non-Disposal Transactions. Of the 351 disposal transactions, 199 transactions, valued at \$58.4 million, were erroneously reported to DRMS as disposal transactions. The erroneous transactions occurred because Navy organizations sent shipment notification transactions to DRMS prior to shipping the materiel and later determined that the materiel either did not qualify for disposal or should have been downgraded to scrap. That practice is contrary to the NAVSUP P-485 requirement to transmit shipping notification transactions to DRMS when materiel is shipped to DRMO.

Reutilization. Materiel for 102 disposal transactions, valued at \$28.7 million, was not shipped to DRMS because it was utilized by other Navy organizations. Reutilization occurs when an organization needs the materiel to meet known or anticipated requirements.

Scrap. Materiel for 60 disposal transactions, valued at \$28.1 million, was not shipped to DRMS because the materiel was subsequently classified as scrap.

Hazardous Materiel and Cylinders Items. Materiel for 27 disposal transactions, valued at \$165,000, was shipped to a hazardous materiel site instead of to DRMO. Navy organizations have a program to screen hazardous materiel and cylinder items for reuse or subsequent disposal.

Pharmaceutical Returns Management Program. Materiel for four disposal transactions, valued at \$15,000, was included in a Pharmaceutical Returns Management Program, which requires that Government organizations send specified prescription, medical, surgical, and diagnostic products to medical contractors instead of to DRMO.

Rejected Transactions. Materiel for six disposal transactions, valued at \$1.4 million, was not in stock at the depot. The depot rejected the six transactions because the materiel was not available for shipment to disposal.

Navy personnel stated that procedures to research and respond to DRMS follow-up transactions that would have detected the problems we identified had not been followed because of a lack of resources, a lack of awareness for monitoring shipments to disposal, problems obtaining proof of shipment information, and non-receipt of DRMS follow-up transactions. None of the 13 Navy organizations that we evaluated or reviewed responded to DRMS follow-up transactions requesting the status of materiel reported as shipped but not received. Reviewing DRMS follow-up transactions is critical in ensuring that materiel in-transit to disposal is properly accounted for and not subject to theft or other forms of fraudulent activity because of loss of asset visibility.

Disposal Shipment Notification Transactions

Navy organizations did not send shipment notification transactions to DRMS, as required by Navy and DoD guidance, because some Navy personnel were not aware of the requirement. Our analysis of DAAS data from May 2002 through April 2003 showed that DRMS sent approximately 85,000 disposal receipt follow-up transactions to all Navy organizations that had not sent shipment notification transactions. The 13 Navy organizations included in our evaluation of disposal transactions accounted for about 13,000 of the 85,000 transactions. The shipment notifications had not been sent because personnel were unaware of the requirement to send DRMS a disposal shipment notification for every DTID. We could not calculate the dollar value of the 13,000 transactions because there were problems with the data in the quantity field of those transactions. If disposal shipment notification transactions are not sent to DRMS, there is no accountability or visibility of the materiel being shipped to disposal because due-ins are not established for materiel that qualify for ICS tracking. An example of the lack of accountability follows.

The Naval Aviation Depot (NADEP) San Diego, California, used the Commercial Asset Visibility, Organic Repair Module to operate its maintenance program. The Commercial Asset Visibility, Organic Repair Module does not interface with the DAAS that transmits disposal shipment notification transactions to the DRMS, and the individual responsible for preparing DTIDs stated that she was unaware of the requirement to submit disposal notification transactions to DRMS. Included in our judgment sample of 700 disposal transactions were 66 transactions, valued at about \$1.25 million, selected from NADEP supply records. Of the 66 transactions, 9 transactions, valued at \$297,033, were not recorded as received at DRMS, and NADEP San Diego personnel could not account for materiel; and five of the nine transactions, valued at \$141,000, involved materiel that was classified as pilferable. There was no accountability or visibility for the \$297,033 worth of materiel because NADEP had not sent disposal shipment notifications to the DRMS.

Disposal Shipment Confirmations

Because of a computer programming error, the Navy's Realtime Reutilization Asset Management (RRAM) Program Office, Mechanicsburg, PA, erroneously sent about 14,400 disposal shipment confirmation transactions (document identifier code ASZ) to DRMS instead of sending disposal shipment notification transactions.

The 14,400 ASZ transactions represent about 52 percent of approximately 27,600 ASZ transactions generated by the Navy during the 12-month period ending April 2003. The RRAM program office provides a real-time visibility inventory of Navy residual assets.

The purpose of an ASZ transaction is to provide status to a DRMS shipment follow-up transaction and results in the cancellation of the ICS due-in at the DRMS. An ASZ transaction confirms to DRMS that there is proof, such as a signed DTID, that the shipment was delivered to DRMO even if there is no evidence of receipt at the DRMS. When an incorrectly generated ASZ transaction is received at DRMS, the transaction is entered into the ICS. However, the ASZ transaction does not establish a due-in, and as a result, the transaction is not subject to the follow-up process. Our review of the RRAM program office's ASZ transactions showed that 214 of the 14,400 ASZ transactions, valued at about \$659,900, would have qualified for inclusion in the ICS had the required shipment notification transactions been sent to DRMS. Erroneous shipment notification transactions result in lost asset visibility. RRAM program office personnel agreed that the computer system needed to be reprogrammed to send the required shipment notification transactions to DRMS.

DRMS ICS Management Data

The Navy and DRMS did not use or evaluate ICS data to monitor in-transit accountability and improve the accuracy of the data in the ICS system. DoD Manual 4000.25-1-M requires DRMS to prepare and send the Military Departments a quarterly in-transit management report. In 1994, the Navy and the Air Force requested to be removed from the distribution list for the report because it contained only summary type statistics, which was not useful. DRMS subsequently discontinued producing the report because DoD was downsizing and the Military Departments did not have the resources required to research the significant number of discrepancies noted in the report.

We agree with the Navy and the Air Force that the report did not provide enough detailed information for it to have been useful to monitor in-transit shipments to disposal. However, detailed information is available in the DRMS management information system and if materiel that is in-transit to disposal is to be properly monitored, both detailed and summary information needs to be reviewed by the shipping organization and monitored by DRMS. By analyzing the DAAS disposal transaction data, we identified the following problem areas that both the Navy and DRMS would have identified if a detailed report had been produced.

- The ICS contained transactions that were less than \$800 and not coded as pilferable or sensitive. According to DRMS personnel, that condition occurred because Navy organizations submitted shipment disposal notifications with incorrect unit prices, which caused the total dollar value of the shipment to exceed \$800. As a result, DRMS follow-up transactions were sent to Navy organizations for disposal transactions that did not meet the criteria for follow-up and could result in unnecessary research by Navy personnel. Our analysis of DAAS data for the 12-month period ending April 30, 2003, showed that 13,925 of the 18,263 shipment confirmation follow-ups that DRMS sent to Navy organizations were valued at less than \$800 and were not sensitive or pilferable.

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- Navy non-disposal supply status transactions intended for organizations other than DRMS were erroneously sent to the DRMS, entered into ICS, and resulted in ICS sending unnecessary follow-up transactions to Navy organizations. The supply status transactions were sent to DRMS because Navy organizations erroneously included a code in card column 54 of the non-disposal supply status transactions, which indicated that the transactions were for disposal. Our analysis of the DAAS database showed that DRMS sent 2,217 follow-up transactions, valued at \$8.47 million, to Navy organizations for non-disposal supply status transactions, which were erroneously sent to DRMS.

Conclusion

There is sufficient guidance and management information to monitor materiel designated for, or sent to, DRMS. However, Navy organizations are either not preparing or are erroneously preparing disposal shipment notifications to DRMS and are not performing the required research on DRMS follow-up transactions. Additionally, neither the Navy nor DLA is using available management information to monitor compliance with the guidance. As a result, Government property is vulnerable to loss and resources may be expended unnecessarily to research erroneous disposal transactions.

Management Comments on the Finding Discussion and Audit Response

Navy Comments. The Navy concurred with those portions of the finding applicable to the Navy. However, the Navy stated that the dollar value impact of the disposal transactions was overstated. The Navy stated that the materiel in question was reported as potential reutilization stock and is valued at 1.9 percent of the last acquisition cost in the Navy Supply Systems Inventory Report. The dollar value of the 700 disposal transactions in the Navy supply system is \$1.7 million, rather than the \$134.4 million we reported, and the dollar value of property vulnerable to loss is \$500,000, rather than the \$39 million we reported.

Audit Response. Regardless of whether the Navy recognizes the latest acquisition cost of \$134.4 million or a devalued reutilization cost of \$1.7 million, the materiel is either useable or pilferable or sensitive materiel and should be controlled through the ICS. We used the standard price of the materiel to determine the disposal transaction values because that is the valuation method that DRMS uses to determine if disposal transactions should be included in the ICS.

Recommendations and Management Comments

1. We recommend that the Commander, Naval Supply Systems Command:

a. Establish controls to ensure that Navy organizations comply with Naval Supply Command Publication P-485, "Ashore Policy," June 1998, requirements to:

(1) Transmit shipment notification transactions to the Defense Reutilization and Marketing Service when materiel is shipped to the Defense Reutilization and Marketing Office and ensure that the data in the shipment notification is accurate.

Management Comments. The Navy concurred, stating that it has taken action to ensure that fleet activities comply with current policy and that it has reissued NAVICP Instruction 4570.1A to clarify current policy and guidance outlined in the NAVSUP P-485 to ensure that shipment notification transactions are transmitted to the cognizant DRMO.

(2) Review and research Defense Reutilization and Marketing Service follow-up transactions for materiel reported as shipped but not received, and respond to the Defense Reutilization and Marketing Service follow-up transactions in a timely manner.

Management Comments. The Navy concurred, stating it has advised fleet activities to comply with the current policy and has reissued NAVICP Instruction 4570.1A to clarify current policy outlined in the NAVSUP P-485. The Navy also stated that it will pass follow-up transactions to the generating activities on a weekly basis.

b. Establish controls to ensure that Navy organizations either demilitarize materiel or provide demilitarization instructions to Defense Logistics Agency depots, prior to requesting the depot to ship materiel to disposal, and respond to depot requests for demilitarization instructions in a timely manner.

Management Comments. The Navy concurred, stating that NAVICP has recently assumed the duties as the Navy Program Manager for Demilitarization and Trade Security Controls. The NAVICP is working with the DoD Program Office, other Services, and Navy System Command and Fleet personnel to identify deficiencies in the demilitarization process. As deficiencies are identified, the NAVICP will seek solutions and funding to rectify the problem.

c. Validate that the Realtime Reutilization Asset Management Program Office reprograms its computer system to ensure that disposal shipment notifications, rather than disposal shipment confirmations, are sent to DRMS for disposal shipments.

Management Comments. The Navy concurred, stating that the RRAM database administrator has confirmed that the RRAM computer programs have been corrected.

d. Request that the Defense Reutilization and Marketing Service provide management reports which identify Navy organizations that are not responding to disposal follow-up transactions for materiel reported as shipped but not received and that are not sending disposal shipment notifications for materiel shipped to disposal.

Management Comments. The Navy concurred, stating that NAVICP will monitor the processing of disposal directives between the fleet and the NAVICP. In addition, the NAVICP has requested reports from DRMS and will provide NAVICP oversight to ensure compliance by fleet activities.

2. We recommend that the Director, Defense Logistics Agency:

a. Establish controls to ensure that Defense Distribution Depot personnel request the required demilitarization instructions for all materiel awaiting disposal instructions and reverse the disposal transactions if the required instructions are not received.

Management Comments. DLA concurred, stating that the Defense Distribution Center is drafting a new instruction letter to Defense Distribution Centers explaining how to handle demil Code F, G, and P items. Additionally, DLA will place the demil instruction in future A-76 Performance Work Statements and modify existing contracts for Defense Distribution Centers that are contractor-operated.

b. Establish controls to ensure that the Defense Reutilization and Marketing Service reviews and analyzes management data to identify Navy organizations that are not routinely preparing shipment disposal notifications or are not routinely responding to follow-up transactions and identify to the Naval Supply Systems Command potential problems with data in the in-transit control system in order for the Naval Supply Systems Command to ensure that Navy organizations comply with disposal procedures.

Management Comments. DLA concurred, stating that the DRMS will collaborate with the Navy to meet the standards set forth in the report.

Appendix A. Scope and Methodology

We performed the audit at 14 Navy activities and 2 commercial contractor facilities:

- Navy Transportation Organization, ATAC (Advanced Traceability and Control), Norfolk, VA;
- Four Naval Fleet Industrial Supply Centers located in Jacksonville, FL; Norfolk, VA; San Diego, CA; and Pearl Harbor, HI;
- Two NADEPS located in Jacksonville, FL and San Diego, CA;
- Three Naval Air Stations located in Willow Grove, PA; Virginia Beach, VA; and Patuxent River, MD;
- Naval Shipyard Norfolk, VA;
- Naval Surface Warfare/Weapons Center Crane, IN;
- Realtime Reutilization Asset Management Program Office, Mechanicsburg, PA;
- Trident Refit Facility, Kings Bay, GA; and
- Two commercial contractors that repair Navy depot level repairable assets: Boeing Aerospace Support Center, Cecil Field, FL and Logistics Services International Jacksonville, FL.

We also visited the following activities during the course of the audit:

- Four DLA distribution depots located in Jacksonville, FL; San Diego, CA; Pearl Harbor, HI; and Norfolk, VA;
- Five DRMOs located in Jacksonville, FL; Norfolk, VA; San Diego, CA; Pearl Harbor HI; and Crane, IN;
- DRMS, Battle Creek, MI;
- Naval Supply Systems Command, Mechanicsburg, PA; and
- NAVICP Philadelphia, PA.

We performed this audit from February 2003 through January 2004 in accordance with generally accepted government auditing standards. The documents we reviewed, which were dated from October 1991 through January 2004, included DoD, DRMS, and Navy disposal guidance; commercial contractor desk procedures; supply and storage records; and DTIDs.

We obtained databases of disposal related transactions from the NAVICP and DAAS. The NAVICP database contained 40,280 issues for disposal transactions for the period March 2002 through February 2003. The DAAS database contained 94,074 disposal shipment follow-up transactions for the period May 2002 through April 2003. For the DAAS data, additional information was obtained from the Federal Logistics Information System to determine the source of supply, the demil code, the controlled inventory item code, the acquisition advice code, and the unit price for disposal transactions. In our analysis of the databases, we judgmentally selected the Navy organizations and commercial contractors to include in our audit tests. In selecting the organizations, we considered the volume and dollar value of DRMS disposal transactions, including both disposal receipt and shipment follow-up transactions.

To determine if materiel designated for, or shipped to, disposal was received at DRMOs or was otherwise accounted for, we selected judgmental samples of 700 disposal transactions, valued at about \$134.3 million, which were processed by 13 Navy organizations and 2 commercial contractors. The sample of 700 transactions included 141 issue for disposal transactions from the NAVICP Philadelphia-supplied database and 207 second disposal shipment confirmation follow-up transactions from the DAAS database. We also judgmentally selected a reverse sample of 352 disposal shipments from supply records of the 13 Navy organizations selected for review. For the RRAM Program Office, we only evaluated why that organization accounted for 14,400 of the 27,600 disposal shipment confirmation transactions that the Navy sent to DRMS.

Use of Computer-Processed Data. We relied on computer-processed data from the DAAS, the Navy's Uniform Automated Data Processing System, the DLA Distribution Standard System, the DRMS Automated Information System and Web Enabled Document Conversion System, the NAVICP Commercial Asset Visibility System, and the ICS. To the extent that we reviewed the data, we found that data in the ICS database was not totally accurate. We identified some transactions that were included in the ICS that were not classified as pilferable and sensitive and were under \$800. These erroneous transactions in the ICS would not preclude the use of the data to meet the audit objective, or change the conclusions in this report.

General Accounting Office High-Risk Area. The General Accounting Office has identified several high-risk areas in DoD. This report provides coverage of the inventory management high-risk area.

Management Control Program Review

DoD Directive 5010.38, "Management Control (MC) Program," August 26, 1996, and DoD Instruction 5010.40, "Management Control (MC) Program Procedures," August 28, 1996, require DoD organizations to implement a comprehensive system of management controls that provides reasonable assurance that programs are operating as intended and to evaluate the adequacy of the controls.

Scope of the Review of the Management Control Program. We reviewed the adequacy of DLA and Navy controls over materiel shipped to disposal. Specifically, we reviewed management controls to ensure that materiel shipped to disposal by Navy organizations was recorded as received at the DRMS or otherwise accounted for.

Adequacy of Management Controls. As defined by DoD Instruction 5010.40, we identified material management control weaknesses in the Navy. Navy organizations were not complying with procedures to ensure that materiel shipped to disposal was not vulnerable to loss or undetected theft. Navy organizations did not review or respond to DRMS follow-up transactions requesting the status of materiel reported as shipped but not received and either did not provide shipment status for materiel that was shipped to disposal or erroneously provided status for materiel that was not shipped to disposal. Additionally, the Navy did not use DRMS management data to monitor in-transit accountability. Recommendation 1. in this report, addressed to the Commander, NAVSUP, if implemented, will correct the material weaknesses identified by this audit.

Adequacy of Management's Self-Evaluation. The Navy did not identify shipments to disposal as an assessable unit and, therefore, did not identify or report the material management control weaknesses identified by the audit.

Prior Coverage

During the last 5 years, the General Accounting Office (GAO) and the Inspector General of the Department of Defense (IG DoD) have issued 3 reports discussing controls over shipment to DRMOs. Unrestricted GAO reports can be accessed over the Internet at <http://www.gao.gov>. Unrestricted IG DoD reports can be accessed at <http://www.dodig.osd.mil/audit/reports>.

GAO

GAO Report No. 01-30, "Implementation Plans to Enhance Control Over Shipped Items Can Be Improved," November 2000

GAO Report No. NSIAD-99-84, "Property Being Shipped to Disposal Not Properly Controlled," July 1999

IG DoD

IG DoD Report No. 99-029, "Property Disposal Management Controls," November 3, 1998

Appendix B. Report Distribution

Office of the Secretary of Defense

Under Secretary of Defense for Acquisition, Technology, and Logistics
Deputy Under Secretary of Defense (Logistics and Materiel Readiness)
Under Secretary of Defense (Comptroller)/Chief Financial Officer
Deputy Chief Financial Officer
Deputy Comptroller (Program/Budget)

Department of the Army

Assistant Secretary of the Army
Auditor General, Department of the Army

Department of the Navy

Assistant Secretary of the Navy (Manpower and Reserve Affairs)
Commander, Naval Supply Systems Command
Commander, Naval Inventory Control Point
Naval Inspector General
Auditor General, Department of the Navy

Department of the Air Force

Auditor General, Department of the Air Force

Combatant Command

Inspector General, U.S. Joint Forces Command

Other Defense Organization

Director, Defense Logistics Agency

Non-Defense Federal Organization

Office of Management and Budget

Congressional Committees and Subcommittees, Chairman and Ranking Minority Member

Senate Committee on Appropriations

Senate Subcommittee on Defense, Committee on Appropriations

Senate Committee on Armed Services

Senate Committee on Governmental Affairs

House Committee on Appropriations

House Subcommittee on Defense, Committee on Appropriations

House Committee on Armed Services

House Committee on Government Reform

House Subcommittee on Government Efficiency and Financial Management, Committee on Government Reform

House Subcommittee on National Security, Emerging Threats, and International Relations, Committee on Government Reform

House Subcommittee on Technology, Information Policy, Intergovernmental Relations, and the Census, Committee on Government Reform

Department of the Navy Comments



DEPARTMENT OF THE NAVY
OFFICE OF THE ASSISTANT SECRETARY
RESEARCH, DEVELOPMENT AND ACQUISITION
1000 NAVY PENTAGON
WASHINGTON DC 20380-1000

MAY 07 2004

MEMORANDUM FOR THE DoD ASSISTANT INSPECTOR GENERAL FOR AUDITING

Subj: COMMENTS ON DODIG DRAFT REPORT ON NAVY CONTROLS OVER
MATERIEL SENT TO DEFENSE REUTILIZATION AND MARKETING OFFICES
(D2003LD-0081)

Ref: (a) DoDIG memo dated March 12, 2004

Encl: (1) DON Comments on Draft DoDIG Audit Report D2003LD-0081

In response to reference (a), enclosure (1) is forwarded. Questions on this response should be directed to CAPT Michael Ahern at (703) 697-2018 or via e-mail at michael.ahern@navy.mil.

A handwritten signature in black ink, appearing to read "Nicholas J. Kunesh".

Nicholas J. Kunesh
Deputy Assistant Secretary of the Navy
(Logistics)

Copy to:
Naval Inspector General (N4)
COMNAVSUPSYSCOM

NAVY COMMENTS TO DODIG DRAFT REPORT OF 12 MARCH 2004
ON NAVY CONTROLS OVER MATERIEL SENT TO DEFENSE
REUTILIZATION AND MARKETING OFFICES
(D2003LD-0081)

Finding 1: Management of the Disposal Process

The controls over materiel designated for or sent to the Defense Reutilization and Marketing Services (DRMS) by the Navy need improvement. Specifically, accurate accountability over property in-transit was lacking. Based on a judgmental sample of 700 Navy disposal transactions, valued at \$134.3 million, for the period of March 2002 to July 2003:

- 349 transactions, valued at \$34.1 million, were properly recorded as received by the DRMS;
- 147 transactions, valued at \$37.7 million, were neither recorded as received by the DRMS nor recorded on accountable supply records (\$32.3 million of the \$37.7 million worth of materiel was located with the assistance of depot personnel);
- 5 transactions, valued at \$4.1 million, were recorded as partial receipts, with some materiel recorded as received (\$2.8 million) and some materiel neither recorded as received nor accounted for on accountability supply records (\$1.3 million); and
- 199 transactions, valued at \$58.4 million, were erroneously reported to the DRMS as disposal transactions.

These conditions occurred because of non-compliance with existing guidance, computer programming errors, and lack of management oversight. As a result, \$39 million worth of Government property not recorded on accountable supply records was vulnerable to loss, and resources could be expended unnecessarily in order to research erroneous transactions.

Navy Comment: Concur with findings. However, the dollar value impact of the disposal transactions is overstated. The material in question is reported as Potential Reutilization Stock in the Navy Supply System Inventory Report (SSIR). This material is valued in the Navy SSIR at 1.9 percent of last acquisition cost. The dollar value of the material in the 700 disposal transactions is reported in the Navy SSIR at \$1.7 million rather than \$134.4

(ENCL 1)

million. The dollar value of property vulnerable to loss is reported in the NAVY SSIR at \$0.5 million rather than \$39.0 million.

Recommendations:

1. We recommend that the Commander, Naval Supply Systems Command:

a. Establish controls to ensure that Navy organizations comply with Naval Supply Command Publication P-485, "Ashore Policy", June 1998 requirements to:

(1) Transmit shipment notification transactions to the Defense Reutilization and Marketing Service when materiel is shipped to the Defense Reutilization and Marketing Office and ensure that the data in the shipment notification is accurate.

Navy Comment: NAVICP concurs with the recommendation and has taken action to ensure fleet activities comply with current policy as outlined in Naval Supply Command Publication P-485, Ashore Policy. NAVICP Instruction 4570.1A of 31 March 2004, was reissued to clarify current policy and guidance to ensure shipment notification transactions are transmitted to the cognizant Defense Reutilization and Marketing Office (DRMO). Advanced copies have been forwarded via email and NAVICP personnel have taken steps to liaison with fleet and supply depot personnel to ensure a basic understanding of updated instructions. We recommend this action be shared with DLA to ensure compliance by Defense Distribution Depot (DDC) personnel since most Navy material is held at DLA managed supply depots. Action is considered complete.

(2) Review and research Defense Reutilization and Marketing Service follow-up transactions for materiel reported as shipped but not received, and respond to the Defense Reutilization and Marketing Service follow-up transactions in a timely manner

Navy Comment: NAVICP concurs with the recommendation and has taken action to advise fleet activities to comply with current policy as outlined in Naval Supply Command Publication P-485, Ashore Policy. NAVICP Instruction 4570.1A of 31 March 2004, was reissued to clarify current policy and guidance. Advanced copies have been forwarded via email and NAVICP personnel have taken steps to liaison with fleet and supply depot personnel to ensure a basic understanding of updated instructions. NAVICP has processes in place to ensure DRMS follow-up transactions, routed to N00383 and N00104, and are passed to the generating activities, on a weekly basis, for response to Defense Reutilization and Marketing Service (DRMS). We

recommend this action be shared with DLA to ensure compliance by Defense Distribution Depot (DDC) personnel since most Navy material is held at DLA managed supply depots. Action is considered complete.

b. Establish controls to ensure that Navy organizations either demilitarize materiel or provide demilitarization instructions to Defense Logistics Agency depots, prior to requesting the depot to ship materiel to disposal, and respond to depot requests for demilitarization instructions in a timely manner.

Navy Comment: Navy concurs with the recommendation. NAVICP has recently assumed the duties as the Navy Program Manager for Demilitarization and Trade Security Controls. Cognizant NAVICP personnel are working with the DoD Program Office, other Services, Navy System Commands and Fleet personnel to identify deficiencies in the demilitarization process. As deficiencies are identified, NAVICP will seek solutions and funding to rectify the problem. NAVICP and DoD have instructions (DODINST 4160.21-M-1, NAVICPINST 4500.45) in place to provide demilitarization guidance and to assist NAVICP item managers/equipment specialists in responding to requests from the fleet/DLA for demilitarization procedures. However, the demilitarization of Navy material ultimately resides with the holding activity. We recommend this action be shared with DLA to ensure compliance by Defense Distribution Depot (DDC) personnel since most Navy material is held at DLA managed supply depots. Action is considered complete.

c. Validate that the Realtime Reutilization Asset Management Program Office reprograms its computer system to ensure that disposal shipment notifications, rather than disposal shipment confirmations, are sent to DRMS for disposal shipments.

Navy Comment: Navy concurs with the recommendation. The Realtime Reutilization Asset Management (RRAM) database administrator at NAVICP Mechanicsburg has confirmed RRAM programs have been corrected. Action is considered complete.

d. Request that the Defense Reutilization and Marketing Service provide management reports which identify Navy organizations that are not responding to disposal follow-up transactions for materiel reported as shipped but not received and that are not sending disposal shipment notifications for materiel shipped to disposal shipments.

Navy Comment: Navy concurs with the recommendation. NAVICP monitors processing of disposal directives to ensure proper actions are taken between fleet activities and the NAVICP. NAVICP Disposal Coordinator, Code 0363 has requested

reports from DRMS to identify fleet activities not responding to follow-up transactions. These reports will provide NAVICP oversight and ensure compliance by fleet activities. We recommend this issue be addressed to the Director, DRMS. Action is considered complete for reporting purposes.

Appendix A: Management Control Program Review

DoD Directive 5010.38, "Management Control (MC) Program," August 26, 1996, and DoD Instruction 5010.40, "Management Control (MC) Program Procedures," August 28, 1996, require DoD organizations to implement a comprehensive system of management controls that provides reasonable assurance that programs are operating as intended and to evaluate the adequacy of the controls.

Scope of the Review of the Management Control Program. We reviewed the adequacy of DLA and Navy controls over materiel shipped to disposal. Specifically, we reviewed management controls to ensure that materiel shipped to disposal by Navy organizations was recorded as received at the DRMS or otherwise accounted for.

Adequacy of Management Controls. As defined by DoD Instruction 5010.40, we identified material management control weaknesses in the Navy. Navy organizations were not complying with procedures to ensure that materiel shipped to disposal was not vulnerable to loss or undetected theft. Navy organizations did not review or respond to DRMS follow-up transactions requesting the status of materiel reported as shipped but not received and either did not provide shipment status for materiel that was shipped to disposal or erroneously provided status for materiel that was not shipped to disposal. Additionally, the Navy did not use DRMS management data to monitor in-transit accountability. Recommendation 1. in this report, addressed to the Commander, NAVSUP, if implemented, will correct the material weaknesses identified by this report.

Navy Comment: To date, DRMS has not provided the management data to monitor in transit material, referenced above, to NAVICP. NAVICP Disposal Coordinator, Code 0363, has requested reports from DRMS to identify fleet activities not responding to follow-up transactions. NAVICP will work any reports provided by DRMS to ensure visibility of assets flowing through the disposal process. NAVICP consistently monitors the processing of disposal directives to ensure a closed loop between fleet activities and NAVICP. However, the loop between the DLA managed distribution depots and DRMO/DRMS is not monitored. We recommend this action be shared with DLA to ensure compliance by DDC personnel since most Navy material is held at DLA supply depots.

Adequacy of Management's Self-Evaluation. The Navy did not identify shipments to disposal as an assessable unit and therefore, did not identify or report the material management control weaknesses identified by the audit.

Navy Comment: NAVICP consistently monitors processing of disposal directives to ensure a closed loop between fleet activities and the ICP and will ensure fleet activities are responsive to DRMS inquiries. NAVICP will identify shipments to disposal as an assessable unit as part of our 2004 management control program.

Defense Logistics Agency Comments



IN REPLY
REFER TO J-3

DEFENSE LOGISTICS AGENCY
HEADQUARTERS
8725 JOHN J. KINGMAN ROAD, SUITE 2533
FT. BELVOIR, VIRGINIA 22060-6221

MAY 18 2004

MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL FOR AUDITING
DEPARTMENT OF DEFENSE

SUBJECT: Navy Controls Over Materiel Sent to Defense Reutilization and Marketing Offices
(DRMOs) (Project No. D2003LD-0081)

This is in response to the subject draft report dated March 12, 2004. If you have any questions, please contact Mr. Melvin Nicholson, (703) 767-6216.


CLAUDIA S. KNOTT
Deputy Director
Logistics Operations

Attachment

**DLA Response to Recommendations in DoD IG Draft Report, Project No.
D2003LD-0081**

2.: We recommend that the Director, Defense Logistics Agency:

a.: Establish controls to ensure that Defense Distribution Depot personnel request the required demilitarization instructions for all materiel awaiting disposal instructions and reverse the disposal transactions if the required instructions are not received.

RESPONSE: Concur, except disposal transactions are being cancelled (not reversed, unless items are owned by the Recycling Control Point) if required instructions are not received.

Defense Distribution Center (DDC) is drafting a new instruction letter to the Distribution Centers explaining how to handle Demil Code F, G, and P items. Additionally, since most DDC sites are contractor-operated, DDC will place the demil instruction request and follow-up requirement in future A-76 Performance Work Statements and modify existing contracts, as necessary.

b.: Establish controls to ensure that the Defense Reutilization and Marketing Service reviews and analyzes management data to identify Navy organizations that are not routinely preparing shipment disposal notifications or are not routinely responding to follow-up transactions and identify to the Naval Supply Systems Command potential problems with data in the in-transit control system in order for the Naval Supply Systems Command to ensure that Navy organizations comply with disposal procedures.

RESPONSE: Concur. The Defense Reutilization and Marketing Service will collaborate with the Navy to meet the standards set forth in the report.

Team Members

The Readiness and Logistics Support Directorate, Office of the Deputy Inspector General for Auditing of the Department of Defense prepared this report. Personnel of the Office of the Inspector General of the Department of Defense who contributed to this report are listed below.

Shelton R. Young
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